

STATE OF ILLINOIS
ILLINOIS COMMERCE COMMISSION

COMMONWEALTH EDISON COMPANY)	
)	ICC Docket No. 10-0527
Petition for approval of an Alternative Rate)	
Regulation Plan pursuant to Section 9-244)	
of the Public Utilities Act)	

REPLY BRIEF ON EXCEPTIONS OF THE PEOPLE OF THE STATE OF ILLINOIS

Janice A. Dale, Chief, Public Utilities Bureau
Karen L. Lusson, Senior Assistant Attorney General
Michael R. Borovik, Assistant Attorney General
100 W. Randolph St., 11th Floor
Chicago, IL 60601
Telephone (312) 814-1136
Fax (312) 814-3212
Email: jdale@atg.state.il.us
Email: klusson@atg.state.il.us
Email: mborovik@atg.state.il.us

TABLE OF CONTENTS

I.	INTRODUCTION	1
II.	RESPONSE TO COMED’S ASSESSMENT OF THE RATE ACEP PROJECTS	3
A.	Urban Underground Facilities Reinvestment (“UUFR”).....	3
1.	The Proposed Order Correctly Found that the Alleged Rate ACEP UUFR Program Benefits Were Insufficient To Satisfy Section 9- 244(b)(2).	3
2.	The Proposed Order Correctly Found that the Alleged Rate ACEP UUFR Program Benefits Were Insufficient To Satisfy Section 9- 244(b)(8).	5
B.	Utility Electric Vehicle (“EV”) Pilot	14
C.	Low-Income Customer Assistance Programs	20
D.	Cost Recovery Mechanism for Future Smart Grid Investments	21
III.	THE PROPOSED ORDER CORRECTLY CONCLUDED THAT THE COMED RATE ACEP PROPOSAL FAILED TO MEET THE STATUTORY CRITERIA.	24
A.	Contrary to ComEd’s Assertions, the Proposed Order Does <i>Not</i> Restrict the Commission’s Authority Under Section 9-244 of the Act.....	25
B.	The Proposed Order Correctly Interpreted Section 9-244(b) of the Act.	28
1.	Rate ACEP Fails Section 9-244(b)(1) of the Act.....	28
2.	Rate ACEP Fails Section 9-244(b)(2) of the Act.....	31
3.	Rate ACEP Fails Section 9-244(b)(7) of the Act.....	32
4.	Rate ACEP Fails Section 9-244(b)(8) of the Act.....	34
IV.	CONCLUSION.....	36

The People of the State of Illinois (“the People”), by Lisa Madigan, Attorney General of the State of Illinois, and pursuant to Part 200.830 of the Illinois Commerce Commission’s (“the Commission”) rules, 83 Ill.Admin.Code Part 200.830, respectfully file their Reply Brief on Exceptions to the Brief on Exceptions (“BOE”) and Exceptions filed by Commonwealth Edison Company (“the Company” or “ComEd”) to the Administrative Law Judge’s (“ALJ”) Proposed Order (“PO”).

I. INTRODUCTION

Not a single witness who testified in response to ComEd’s proposed Rate Accelerated Customer Enhancements Pilot (“Rate ACEP”) tariff, including the Commission Staff, believed the proposal filed by ComEd constituted a serious, legitimate attempt to create an alternative way of setting rates and modernizing the ComEd electric grid. All parties who analyzed the statutory requirements of Section 9-244 of the Public Utilities Act (“the Act”) against the Company’s rate proposals concluded that the Rate ACEP proposal failed to satisfy the essential requirements of the statute necessary to gain Commission approval of the plan. As the People noted in their briefs in this case, rather than offering a proposal that could legitimately be described as “alternative regulation,” ComEd’s proposed Rate ACEP authorizes business-as-usual rate cases and additional, piecemeal recovery of certain capital and operating expense costs between rate cases.

The Proposed Order accurately reflected the parties’ positions, correctly interpreted Section 9-244 of the Act, and applied the law to the facts of the proposal and the overall record evidence. The Proposed Order rejected the Rate ACEP proposal, concluding that the plan satisfied neither section (a) or (b) of Section 9-244 of the Act. In response, ComEd’s BOE launches an over-the-top, inaccurate assessment of the effect of the Proposed Order’s

conclusions, arguing that the ALJ's ruling "slams the door on regulatory innovation in Illinois" and would "sharply restrict the Commission's ability to approve future alternative regulation proposals." ComEd BOE at 1-2. Continuing its dramatic summation of the case – including a cryptic reference to a recent speech of President Obama that recognized "American ingenuity" -- the Company further opines that the goal of network modernization "will require the Commission to be flexible and innovative." ComEd BOE at 2. Under ComEd's proposal, however, such Commission flexibility and innovation would necessarily include ignoring the law. The Commission should reject this rhetoric and the Company's invitation to ignore the mandates of Section 9-244 of the Act.

The Proposed Order got it exactly right. Rather than ease the regulatory process, provide tangible benefits to ratepayers and incent the Company to operate efficiently, all while recovering its costs and earning a reasonable profit, the ComEd Rate ACEP proposal would merely increase customers' rates on a piecemeal basis for recovery of specific investments and expenses while actually *increasing* the regulatory burdens associated with traditional rate of return regulation. ComEd has not proposed a new regulatory framework driven by changes in ComEd's overall financial performance, revised methods to determine revenue requirements, sharing of earnings or any other meaningful expansion of performance incentives. Rate ACEP is also not performance based ratemaking, as it would not attempt to measure the utility's performance against any overall cost-efficiency or service quality metrics or standards that could justify penalties or rewards of any consequence to the Company or its ratepayers. Adoption of Rate ACEP would only produce rate increases to consumers, for discrete infrastructure investments projects and new O&M expenses, and higher revenue for ComEd than would exist under traditional rate of return regulation. ComEd admits this in its BOE when it bristles at any

comparison of its plan with typical alternative regulatory forms listed in Section 9-244(a), and instead points out that it is asking the Commission to examine its proposal under Section 9-244(b) within the context of “which method of providing those services – traditional or alternative regulation – will result in lower rates ‘for the services covered by the program.’” ComEd BOE at 3, citing 220 ILCS 5/9-244(b)(1). The problem, however, as the Proposed Order correctly concluded, is that the Rate ACEP project proposals are not “services” in any legitimate interpretation of the word, and, as such, the plan fails to satisfy the requisite criteria for adoption of an alternative regulatory plan specified in Section 9-244 of the Act.

For the reasons discussed below, the Commission should reject ComEd’s analysis of its Rate ACEP proposal and its claims about the precedential effects of the Proposed Order, and adopt the ALJ’s well-supported conclusions and sound analysis.

II. RESPONSE TO COMED’S ASSESSMENT OF THE RATE ACEP PROJECTS

A. Urban Underground Facilities Reinvestment (“UUF”) ”

1. The Proposed Order Correctly Found that the Alleged Rate ACEP UUF Program Benefits Were Insufficient To Satisfy Section 9-244(b)(2).

In its BOE, ComEd argues that the Proposed Order misinterpreted the Act when it concluded that the UUF program under Rate ACEP “in no way satisfies...the requirements that must be met for Commission approval of Rate ACEP under Section 9-244 of the Act.” PO at 75. ComEd claims that “the Proposed Order applies Section 9-244(b)(2) is (sic) if it required a showing that the ‘benefits...are not likely to accrue *for UUF performed under traditional regulation.*’” ComEd BOE at 9 (emphasis in original). This argument is spurious because ComEd’s selective citation to the argument mischaracterizes the particular conclusion cited and the rationale applied. The relevant passage of the Proposed Order states:

The Commission does not find any support in the record for the proposition that UUFR performed under Rate ACEP provides any benefits that are not likely to accrue for UUFR performed under traditional regulation. The Commission recognizes that ComEd has said it will not undertake the UUFR project unless Rate ACEP is approved, but the Commission does not find this persuasive. If Staff is correct that this project is necessary to ensure adequate reliability for Illinois ratepayers, then ComEd should complete it, with or without Rate ACEP. The Commission rejects ComEd's argument that this would be an unfunded mandate. The ability of a utility under traditional regulation to recover its reasonable and prudently incurred costs for necessary, used and useful investments is long-standing and if UUFR is required to provide adequate reliability there is no basis for assuming the associated costs will not be recovered from ratepayers.

Proposed Order at 76. While ComEd suggests a comparison to traditional regulation is inappropriate when analyzing its Rate ACEP proposal, in fact, the statute requires the Commission to compare the alleged benefits of the program with that which would occur "in the absence of the program." Among the eight criteria that must be satisfied under Section 9-244 is subsection (b)(2), which states:

The Commission shall approve the program if it finds, based on the record, that:
... (2) the program is likely to result in other substantial and identifiable benefits that would be realized by customers served under the program and *that would not be realized in the absence of the program*;

220 ILCS 5/9-244(b)(2) (emphasis added). Traditional regulation is the regulatory environment "in the absence of the program." While Staff believed the Commission should order the Company to undertake the UUFR project with or without Rate ACEP, the Proposed Order correctly concluded that this docket was not the proper forum for such a Commission directive. However, the Proposed Order rightly noted:

The ability of a utility under traditional regulation to recover its reasonable and prudently incurred costs for necessary, used and useful investments is long-standing and if UUFR is required to provide adequate reliability there is no basis for assuming the associated costs will not be recovered from ratepayers.

Proposed Order at 76. The Proposed Order correctly observed that ComEd could and should invest in UUFR under traditional regulation, without worry that those costs would be deemed

imprudent. However, the notion that ratepayers should be charged a premium under a Rate ACEP plan whose alleged benefits relied on a false benchmark metric – ComEd’s own budget estimates – was soundly rejected. The Proposed Order correctly observed:

Because of the risk of inflated budgets and the cap on O&M savings, it is not apparent to the Commission that the record supports a finding that ComEd’s UUFR proposal appropriately reflects an equitable sharing of the net economic benefits. In fact, ComEd provided no quantitative analysis to support its assertion that Rate ACEP’s, and in particular UUFR’s, net economic benefits are being equitably shared with ratepayers. The Commission notes that the AG states that Rate ACEP “would not account for either the avoided cost of the normal level of ongoing UUFR replacement that is embedded in test year rate cases or for any prospective O&M savings that may result from the acceleration of UUFR replacements and reduced outage response costs” AG Ex. 1.0 at 40. The Commission is likewise concerned that UUFR benefits are not shared with customers until the next rate case.

PO at 76. The Proposed Order further found that the UUFR project under the Rate ACEP budget forecast process “could easily be manipulated to allow ComEd to declare a project complete in order to come in under budget.” PO at 77. All in all, ComEd failed to show that the Rate ACEP plan of requiring ratepayers to pay a premium for an ill-defined investment plan failed to qualify as the kind of “substantial and identifiable benefits that would be realized by customers served under the program and that would not be realized in the absence of the program.” There was nothing improper about the Proposed Order’s interpretation of Section 9-244 or the facts applied to the law.

2. The Proposed Order Correctly Found that the Alleged Rate ACEP UUFR Program Benefits Were Insufficient To Satisfy Section 9-244(b)(8).

ComEd also takes exception with the PO’s conclusion that the UUFR program under Rate ACEP failed to satisfy the requirement under Section 9-244(b)(8) that it provide “an equitable sharing of any net economic benefits between the utility and its customers to the extent the program is likely to result in such benefits.” PO at 76. ComEd claims that the Proposed Order failed to “discuss or give any weight” to the Rate ACEP’s proposal to share half of any

capital carrying costs savings generated by ComEd completing the programs for less than the Commission-approved budget and “all of the benefit” of reduced O&M costs. ComEd BOE at 10-11. ComEd further claims that this benefit is “more favorable to customers than the 50/50 sharing mechanism in the *Nicor Alt Reg Order*.” *Id.* at 11.

The facts in evidence and the analysis of the witnesses who assessed these purported benefits belie that conclusion. The Proposed Order specifically acknowledged the UUFR sharing proposal, but correctly determined that ComEd proposed budgets and project descriptions are inappropriate benchmarks for analyzing when sharing provisions are appropriately activated. PO at 76-77. Both the timing of sharing benefits (the next rate case) and the ability to deem a project completed remain completely within the control of ComEd, thereby highlighting the potentially elusive nature of any claimed benefit or savings. This flaw in the proposal is specifically highlighted in the Proposed Order’s Analysis and Conclusion:

It would be near impossible to determine when the UUFR project is complete because there are no specific scope of work parameters defined before the budget is established. The Commission understands that the proposed project is to replace 2,400-3,600 manholes and 25-37 miles of cable. The Commission is concerned that this is a huge range that could easily be manipulated to allow ComEd to declare a project complete in order to come in under budget.

PO at 77. This inherent defect in Rate ACEP cannot be cured by simply pointing to a 50/50 sharing mechanism. Likewise, ComEd’s arguments that there was no specific evidence of budget inflation in the case (ComEd BOE at 11-12) does not cure the inherent unreliability of using ComEd-proposed budgets as a sharing benchmark. The ALJ agreed with the Commission Staff and other witnesses who pointed out that the role of evaluating what and how much plant investment should be made is historically the responsibility of utility management, who are in a much better position to evaluate the costs and benefits of discrete technology choices and plant investment optimization, as opposed to regulators who are unlikely to have in their possession all

of the information, personnel and other resources necessary to independently conduct such evaluations. *See, e.g.*, AG Ex. 1.0 at 34. The evidence that supported that conclusion included:

- AG witness Brosch pointed out that the Rate ACEP budget process would never reduce ComEd revenues relative to traditional regulation, but would simply limit surcharges to customers to 105 percent of approved budgeted cost levels. Alternatively, if actual capital spending is less than the approved budget by more than five percent (actual costs less than 95% of budget), ComEd would be allowed to retain half the savings, effectively overcharging customers on a 50/50 basis for carrying costs on budgeted capitalized costs that were *not* incurred. This so-called incentive would do little more than encourage ComEd to (1) overstate the budgeted costs presented to the Commission for approval and (2) constrain actual program expenditures, which are admittedly discretionary to start with, so as to ensure that budgets are met or beaten (to the potential detriment of ratepayers and benefit to the Company). AG Ex. 1.0 at 19-20.
- Staff witness Rearden likewise rejected the notion that limiting recovery of O&M expenses to 95% of estimated costs sufficiently protects ratepayers against paying excessive costs because Staff and intervenors are not likely to effectively verify the budget. He pointed out that ComEd has an incentive to overestimate the budget, and Staff and any other possible party possess less information concerning ComEd's costs and operations than ComEd does. In addition, Rate ACEP preserves ComEd's ability to seek any O&M costs not recovered under Rate ACEP in a rate case. Staff Ex. 8.0, p. 14.
- The incentive scheme for capital investment cost recovery is similarly flawed. The risk that ComEd under-recovers its investment costs is not symmetric with the possibility that it generates savings (i.e., ComEd incurs costs below 95% of the budget), according to Staff. Thus, the consequences that ComEd would face for exceeding the budget can be, from ComEd's point of view, remedied, but ratepayers have much less protection in case the project's cost is over-estimated. Under Rate ACEP, ComEd can seek to recover overruns in future rate cases, so even if ComEd spends more than it can initially recover, it can apply to recapture the shortfall in a rate case. Second, as discussed above, it has an incentive to make the capital budget larger. A larger budget means ComEd is less likely to exceed it and more likely to come in under budget, thus granting ComEd a share of the dubiously estimated savings. Staff Initial Brief at 14, citing Staff Ex. 8.0 at 16.
- Under Rate ACEP, ComEd has an incentive to declare a project complete when it nears the 95% and 105% of the budget, even if it is not finished. While ComEd shareholders share in savings for costs below 95% of the budget, there is a deadband from 95% to 105% of the budget, in which ComEd is entitled to recover exactly what it spends. Above the deadband, ComEd must refund the difference between actual expenditures and the budget. If ComEd's expenditures are close to 105%, it should declare the project complete, to avoid refunds. On the other hand, when its expenditures are below 95% of the budget, ComEd has an incentive to declare that the project is complete in order to generate returns above cost from the sharing mechanism. Staff Initial Brief at 15, citing Staff Ex. 1.0R at 23; Staff Ex. 8.0 at 16.

The Proposed Order aptly acknowledged these defects in the Rate ACEP budget metrics, noting, “it is difficult for the Commission to imagine how oversight of a budget and construction decisions would be a constructive use of Staff’s, and Intervenor’s, time and resources.” PO at 77; *see also* PO at 50-51. This inherent defect in the Rate ACEP tariff makes the sharing claim unreliable. ComEd may have not liked the conclusion of the Proposed Order, but the ruling fairly evaluates and acknowledges the proposed sharing mechanism, as highlighted in the multiple passages quoted above.

Moreover, even if it failed to discuss the proposed sharing mechanism, which it did not, Commission findings need only be sufficiently specific to allow for an informed judicial review. Particular findings as to each evidentiary fact or claim are not required. *United Cities Gas v. Illinois Commerce Comm’n*, 47 Ill.2d 498 (1970). The Commission is required to make findings only as to those facts which are essential to its determination. *Citizens Utilities Co. v. Illinois Commerce Comm’n*, 49 Ill.2d 458, 463 (1971). The Proposed Order more than satisfies that legal standard.

ComEd also argues that the Proposed Order implicitly concluded that Section 9-244(b) requires a specific “quantitative analysis” related to benefit sharing claims, contrary to the plain language of the statute. ComEd BOE at 11-13. Again, the Company exaggerates the breadth and meaning of the ALJ’s conclusions based on selective quotations. Here again is the referenced conclusion, in its full context:

Because of the risk of inflated budgets and the cap on O&M savings, it is not apparent to the Commission that the record supports a finding that ComEd’s UUFR proposal appropriately reflects an equitable sharing of the net economic benefits. In fact, ComEd provided no quantitative analysis to support its assertion that Rate ACEP’s, and in particular UUFR’s, net economic benefits are being equitably shared with ratepayers. The Commission notes that the AG states that Rate ACEP “would not account for either the avoided cost of the normal level of ongoing UUFR replacement that is embedded in test year rate cases or for any prospective O&M savings that may result from the

acceleration of UUFR replacements and reduced outage response costs” AG Ex. 1.0 at 40. The Commission is likewise concerned that UUFR benefits are not shared with customers until the next rate case.

Proposed Order at 76. The Proposed Order’s reference to a “quantitative analysis” is an acknowledgement that the alleged benefits of the UUFR program, under Rate ACEP are neither 1) easily discernible, given the flawed budget benchmark and that ratepayers would pay an extra charge for UUFR in addition to amounts that which would have been subsumed in test year ratemaking, nor 2) guaranteed to flow to ratepayers unless and until ComEd files a rate case. Given these realities of the Rate ACEP mechanism, the Proposed Order rightly concluded that a “quantitative analysis” that demonstrated the budget metric was a reliable benchmark for producing the perceptible benefits was lacking in the proposal. PO at 76.

ComEd suggests that through the budget’s reflection of an assumed productivity gain and by charging customers for only 95 percent of the incremental O&M expenses for the programs through Rate ACEP, customers have somehow automatically “saved” money relative to what they would have paid under traditional regulation. ComEd BOE at 11, 32-34. For consumers to save, however, it would be necessary to assume that 100 percent of the same incremental O&M in each future year would be incrementally recoverable under traditional regulation between test years – which is clearly not how traditional, test year regulation functions. In addition, the ComEd claim that ratepayers will automatically “save” through the budget presented assumes that 1) Staff and intervenors can easily verify the budget and amounts spent for the discrete projects; and 2) that there is a benefit in having ratepayers pay an additional charge for the UUFR project in the first place based on vague claims of increased reliability. The Proposed Order rightly concluded that those assumptions are unproven, as noted above, noting that 1) ComEd failed to propose a performance standard for the UUFR project based on measures

related to improved reliability rather than budget; and that 2) “(w)hether the Company can complete this project under budget has nothing to do with the reliability of its system and ...is an unsuitable performance standard in the context of alternative regulation.” PO at 77; *See also* PO at 50-51.

Again focusing on the Proposed Order’s reference to a “quantitative analysis,” ComEd also claims that courts have declared imposing quantitative evidentiary standards “for demonstrating after-the-fact benefits inappropriate when the statute does not call for one, citing *Illinois Power Co. v. Illinois Commerce Comm’n*, 339 Ill.App.3d 425, 439-40 (1st Dist. 2003) (“*Illinois Power*”). ComEd BOE at 12. The *Illinois Power* case is inapposite to the instant docket and not relevant to the Proposed Order’s conclusions. *Illinois Power* involved a Commission decision related to a purchased gas clause reconciliation under Section 9-220(a) of the Act. In its reversal of a Commission decision that relied upon a present-value-of-future-revenue requirements (“PVRR”) analysis to deem imprudent a company decision to retire a particular propane plant, thereby affecting gas supply costs, the Appellate Court ruled that section 9-220(a) of the Act does not set forth any specific type of analysis that a utility must perform to show that its costs are prudent. *Illinois Power*, 339 Ill.App.3d at 439-440. The Court specifically found that the Commission created an *after the fact* standard of care a reasonable person should have followed in early 2000 when deciding whether to retire the propane plant at issue, and it applied it in hindsight to judge the prudence of Illinois Power's actions.

The Proposed Order argues for no such hindsight review or particular quantitative methodology. Instead, it acknowledges the inherent unreliability of the budget benchmark itself and the inability to evaluate when a project is, in fact, complete, as the inherent flaw in the Rate ACEP tariff and the UUFR project. ComEd’s claims at pages 16-19 that the UUFR budget and

work plan provided reliable, specific quarterly work and budget amounts in no way diminishes the Proposed Order's finding. The point ComEd fails to acknowledge is that these numbers cannot be validated as reasonable benchmarks. As the Proposed Order correctly noted, "it is impossible to approve a reasonable budget when the scope of the work is so fluid and undefined. Indeed, because UUFR involves testing, which has not been undertaken, followed by a decision on what level of work is required, the Commission believes the nature of UUFR makes it extremely difficult to assess the reasonableness of ComEd's UUFR budget." PO at 76.

What *is* certain is that ComEd customers would be charged from \$4.4 million to \$5.2 million per calendar quarter, beginning in the fourth quarter of 2011, with cumulative estimated charges through January of 2013 totaling \$24.1 million¹, for projects that ComEd's own management deemed were not cost-effective to include in annual capital budgets. *See* Tr. at 69-73; AG Reply Brief at 16-18. These illustrative calculations, provided by ComEd, likewise do not reflect any potential future expansion in the scope of the four programs offered at this time – something for which the Rate ACEP tariff specifically provides.² The bottom line is that customers will pay more than what they pay now for alleged benefits that are illusory at best.

ComEd further criticizes the Proposed Order's reliance on testimony from AG witness Michael Brosch that Rate ACEP "would not account for either the avoided cost of the normal level of ongoing UUFR replacement that is embedded in test year rate cases or for any prospective O&M savings that may result from the acceleration of UUFR replacements and

¹ Actual timing would depend upon the timing of Commission approval of programs and ComEd's rate of actual spending. Charges through Rate ACEP would continue and grow until ComEd's next base rate case provides an opportunity to include the cumulative investments within test year approved utility rates.

² ComEd's Rate ACEP tariff is open ended, providing for future expansion to include, "...any new or modified accelerated customer enhancement program proposed by the Company and approved by the ICC." AG 1.0 at 16, citing the Rate ACEP tariff.

reduced outage response costs.” PO at 76, citing AG Ex. 1.0 at 40. The Company asserts that the “proactive work performed under the proposed UUFR project is completely incremental and additional to the ongoing emergent and reactive maintenance work” ComEd performs. This argument ring hollow. ComEd’s claim that the UUFR program is uniquely incremental is a false distinction. When viewed in isolation, any capital work can be called incremental. The point Mr. Brosch was making is that ratepayers are continuously funding UUFR investment under traditional regulation. UUFR is a continuous process that does not lend itself to piecemeal charges or a special accounting process, as the Proposed Order correctly concluded.

ComEd also downplays the Proposed Order’s concern that “UUFR benefits are not shared with customers until the next rate case” (PO at 76, citing AG Ex. 1.0 at 40), arguing that there are no “appreciable non-storm related outage response costs potentially resulting from UUFR”, and that the real benefit lies in the Company’s proposal for a means of sharing capital costs associated with UUFR. ComEd BOE at 15. While ComEd minimizes the savings that would not be recognized by Rate ACEP, it cannot be disputed that when the company replaces old plant, it is avoiding future outages and some level of repair costs. Rate ACEP, however, fails to recognize that reality in the form of shared customer benefits.

The bottom line is that notwithstanding ComEd’s claims of budget and capital costs savings, there is no specific information provided in the Company’s filing identifying or quantifying any benefits, nor any showing that such benefits are not achievable under traditional regulation that would justify a Rate ACEP surcharge, over and above rates set in traditional rate cases. As noted by Staff witness Harry Stoller, the Company “does not explain why customers should pay a premium for service quality that is not required by law or any other standard he has identified.” Staff Ex. 7.0 at 6. In addition, the Company provided no evidence that the proposed

UUFR program “will, in fact, actually move ComEd’s delivery service quality beyond what is required to meet service requirements.” *Id.*

Finally, in yet another distortion of the limits of traditional ratemaking, ComEd complains about the Proposed Order’s conclusion that there is no basis to assume that any of the costs associated with the UUFR project would not be recovered under traditional regulation. ComEd BOE at 20, 32. The Company opines that “the return on and of UUFR investments between the time made and the inclusion of such costs in new rates is forever lost under traditional regulation” and that it would be difficult or include “proactive O&M costs” into either an historical or future test year. These arguments, again, ignore the realities of the ratemaking process that has been in place and functioning for more than a century. The fundamental basis for traditional utility regulation is that, in the absence of competitive markets to determine pricing for an essential public service, just and reasonable utility rates should be determined based primarily upon the utility’s prudently incurred costs to provide such monopoly services. A critical element of traditional test period regulation is the incentive created for management to control and reduce costs, so as to maximize the opportunity to actually earn at or above the authorized return level *between rate case test periods*. Traditional test year regulation is not continuous regulation, because prices established in a rate case are normally fixed for a period of years. Changes in actual costs or sales levels between rate cases can increase or decrease a utility’s profit levels before such changes can be translated into revised prices after a “next” rate case. This passage of time between rate cases, commonly referred to as “regulatory lag,” serves as an efficiency incentive and moderates the counter-incentive that results when prices are based upon costs to serve. AG Ex. 1.0 at 6-7. The ComEd complaint, accordingly, is a hollow one.

For all of the above reasons, the ComEd arguments related to the UUFR project in its BOE should be rejected. The Commission should adopt the Proposed Order's conclusions and analysis in its Final Order.

B. Utility Electric Vehicle ("EV") Pilot

ComEd disagrees with the PO "in both its analysis and conclusion regarding the Electric Vehicle ("EV") Pilot project." ComEd BOE at 20. In support of their position the Company contends: 1) ComEd's budget is not inflated; and 2) ComEd cannot "substitute" cheaper equipment to "game" its budgets. *Id.* at 21-26.

The PO, however, got it right stating in part:

...a fundamental flaw in the proposal to measure ComEd's actual performance against a pre-approved budget. It appears to the Commission that in at least some instances, **ComEd will have an incentive to act in a manner that is in its shareholders economic interests and, at the same time, contrary to customers' economic interests.**

Proposed Order at 92 (emphasis added).

The ComEd EV Pilot under Rate ACEP Provides a Disincentive to Lower Customer Costs as Compared to Traditional Rate of Return Regulation

The People agree with the PO that the pre-approved budget process is flawed and unlikely to result in "lower rates than otherwise would have been in effect under traditional rate of return regulation." 220 ILCS 5/9-244 (b)(1); and unlikely "to result in other substantial and identifiable benefits that would be realized by customers served under the program and that would not be realized in the absence of the program." 220 ILCS 5/9-244 (b)(2).

ComEd attempts to support its assertion that its budget is not inflated by stating:

Ironically, while accepting the unreasonable and illogical view that the utilities will necessarily act on economic incentives to improperly inflate publicly reviewed budgets, the Proposed Order simultaneously fails to find that utilities would act on legitimate incentives to share in increased efficiencies and cost savings under rate sharing mechanisms such as Rate ACEP."

ComEd BOE at 21.

It is naive to believe, however, that ComEd would not *act on economic incentives* as they describe above . As the PO stated, “ComEd will have an incentive to act in a manner that is in its shareholders economic interests and, at the same time, contrary to customers’ economic interests.” PO at 92. Unfortunately, when the Company does act on those incentives to inflate its budgets, it does not necessarily follow that it will also act to share increased efficiencies and cost savings under the ComEd proposed rate sharing mechanism. In essence, these two incentives are mutually exclusive.

Staff witness Dr. David Rearden discusses why Rate ACEP is fatally flawed. In support of this, Dr. Rearden states:

I recommend that the Commission reject Rate ACEP. A key component of Rate ACEP is that ComEd determines its ultimate cost recovery by reference to a **budget pre-approved by the Commission** for each project financed by Rate ACEP. As I argue below, this is a **grave structural flaw that I believe to be impossible to overcome** even with modifications to Rate ACEP.

ICC Staff exhibit 1.0 at 3.

Also, Dr. Rearden describes why Rate ACEP misaligns Company incentives, or rewards ComEd to maintain higher rates than would be seen under traditional rate of return regulation. For example, Dr. Rearden describes why “ComEd has a strong incentive to overestimate the budget” (*Id.* at 19-20), or that “there appears to be nothing in Rate ACEP to prevent ComEd from strategically declaring a project complete to reap benefits from the incentive scheme. *Id.* at 22.

In contrast, traditional regulation maintains certain safeguards to prevent an unreasonable risk to ratepayers. As Dr. Rearden opines:

A prudent utility plans the best it can and invests efficiently. If the utility

cannot justify its expenditures, then it can be at risk for a disallowance. This is a very important incentive for the utility and an important safeguard for ratepayers.

Id. at 8

Clear evidence of the issues generally described by Staff witness Dr. Rearden can be identified as problems for the EV pilot. In particular the misaligned incentives and significant ratepayer risk relates to Company-developed budgets and questionable benefits at best. As Staff witness Jennifer Hinman states:

The **Company has every incentive** [citation omitted] **to inflate the budget** proposed to the Commission to **stay far enough under budget to complete the program** and thereby **profit substantially**. **Ratepayers** would be **harmed by these inflated budgets** because they would have to pay the resulting higher rates.

ICC Staff Ex. 2.0 at 3 (emphasis added).

ComEd attempts to minimize, both in its BOE and previously in briefs, the discrepancy between the Company-developed budget and the cost evaluation conducted by Staff witness Jennifer Hinman. For instance, the Company first opines, “[t]here was some dispute concerning the estimated costs of the various vehicles and other facilities to be used for the pilot.” ComEd Brief at 26. Next, the Company states, “ComEd explained that bucket truck costs vary widely depending on the type of mounted aerial equipment as well as other vehicle components such as lighting and storage compartments. McMahan Reb., ComEd Ex. 7.0, 2:36-3:56.” *Id.* Remarkably the Company goes on to conclude that the record shows that ComEd’s budget for the EV Pilot is reasonable. *Id.*; BOE at 20-26. The Proposed Order rightly rejected that assessment.

The Company’s Budget Reveals Inflated Costs, Lack of Transparency and Higher Costs to Rate Payers.

While the Company is steadfast in its belief that the EV Pilot budget is reasonable, a comparison of this budget to Staff’s detailed analysis reveals a different story. In fact, Ms.

Hinman, in reviewing the Company's budget related to the EV pilot, ICC Staff Exhibit 2.0 and 9.0, determined the Company inflated its budget by over twenty percent. *Id.* at 22. The ComEd BOE, however, continues to support the Company's proposed budget and opines, "the Proposed Order's conclusions regarding the EV Pilot budget are contrary to the record and not well reasoned." ComEd BOE at 26. The record in this case, however, exposes the fact that the EV pilot under Rate ACEP gives the Company tremendous control without transparency over certain information necessary to identify, verify, or double check the Company's budget. In one case, Mr. McMahan supported his cost estimates by stating, "per-unit costs for charging infrastructure are based on estimates generated from conversations with charging infrastructure providers, and not actual quotes for work." ComEd Ed. Ex. 7.0 at 13.³ How can Staff or intervenors verify these statements?

Additionally, Ms. Hinman states:

Details such as model numbers and technical specification that are missing from the proposed budgets may have significant impacts on ComEd's final investment expenditure amounts. ComEd appears to be able to choose to complete a program under budget, especially if it overestimates the cost to purchase assets and ends up purchasing different cheaper models.... Different models and manufacturers of virtually the same type of vehicle have significant differences in costs. When the monetary incentive is tied to a budget, the Company will have an incentive to spend under budget. The more inflated the budget, the greater the profit opportunities are, and the more likely it is that ratepayers will be paying higher rates under the Alt Reg mechanism than they would otherwise pay under traditional rate of return regulation.

ICC Staff Exhibit 2.0 at 9.

Another example of the budget metric frustration relates to tax credits and grants that were not taken into account in the initial EV pilot budget. While Mr. McMahan accepted "the

³ Staff witness Ms. Hinman in reviewing vehicle cost estimates provided by the company stated, "[the manufacturers' websites have the prices of new vehicles protected such that only members/previous customers can view the prices." ICC Staff Exhibit 2.0 at 7; Footnote 3.

recommendation of Staff witness Hathhorn to modify the Rate ACEP tariff to account for any grants or credits that ComEd uses” (ComEd Ex. 7.0 at 11), it did so only after Staff pointed out the problem. Additionally, the problems with the Company developed budget were succinctly described by Staff in that⁴:

ComEd may have access to price discounts of which only it is aware. Such discounts would reward ComEd not for superior efficiency, but rather for its superior knowledge as a market participant. The fact that Staff’s research found lower asset prices which may be more reasonable points to the intractable nature of calculating a fair budget to be used to measure Company performance.

Thus, the underlying assumptions behind the EV pilot budget cannot be verified. Furthermore, ComEd attempts to portray their proposal as allowing “the Commission and the public to have a greater say in how ComEd adapts its electric delivery system to a changing world before those investments are made.” ComEd BOE at 4. In reality however, ComEd has dictated what they intend to do under the EV Pilot, but made no substantive changes to the budget or the EV Pilot at large in spite of what Staff or various intervenors recommended. This hardly represents the kind of collaborative process the Company has described. As the PO succinctly stated:

Because of the problems with the budget process, ComEd has not shown that the proposed EV pilot, which the Commission finds to be poorly defined, should be be [sic] funded through rate ACEP.

PO at 93.

Assessing a discrete charge through Rate ACEP for an EV Pilot is unnecessary, will result in higher rates and provides unlikely benefits to ratepayers.

⁴ See also, AARP Ex. 1.0 at 19; AG Ex. 1.0 at 33-34, 44, 47-48; AG Ex. 3.0, at 3; IIEC Ex. 1.0-C at 10, 16-17; IIEC Ex. 2.0 at 9-10

According to ComEd, the Company currently owns 10 converted plug-in hybrid electric vehicles (Toyota Prius); and nine hybrid electric bucket trucks (International/Eaton). ICC Staff Exhibit 2.0 at 7; Staff Ex. 9.1, Part 1. Notably, in his rate case testimony in pending Docket No. 10-0467, ComEd witness McMahon addresses ComEd's fleet of approximately 3,300 vehicles, including various hybrids, biofuel and flex-fuel vehicles.⁵ The 59 incremental vehicles proposed under the EV Pilot program represent replacement of less than two percent of the entire fleet.⁶ In the normal course of business, ComEd would expect to replace at least 150 to 200 vehicles annually, given its depreciation accrual rates of 11.59% for passenger cars, and accrual ranges from 5.72% to 12.04% for various types of trucks.⁷

As explained by AG witness Brosch, there is nothing special about the EV pilot, as it could readily be absorbed into ComEd's routinely large need to deploy replacement vehicles each year. However, rather than simply integrating the proposed EV Pilot into normal vehicle replacements, Rate ACEP clearly envisions shifting all the up-front costs and risks of the Company's planned EV research project onto customers, even though any benefits from this pilot are far from certain. *Id.* at 27-28; AG Ex. 3.0 at 11.

Staff witness Jennifer Hinman concurred that it is unnecessary and not beneficial to ratepayers to recover costs associated with EVs through the Rate ACEP proposal. She points out

⁵ AG Ex. 1.0 at 27. Docket No. 10-0467; ComEd Ex. 9.0 Rev. at 44-45.

⁶ ComEd Ex. 2.0, page 5, shows the planned quantity of EV vehicles for the Pilot would include 45 plug-in cars, 8 cargo/service vehicles, 4 hybrid bucket trucks and 2 PHEV digger-derrick vehicles.

⁷ ComEd's rate case filing in Docket No. 10-0467 includes disclosure of depreciation accrual rates under Part 285.305 (e); AG Ex. 1.0 at 27.

ComEd's current fleet is currently comprised of mostly alternative fueled vehicles, noting that ComEd's website states that the Companies green fleet is currently comprised of the following vehicles:

- 1,774 trucks that use biodiesel fuel (20% soybean oil, 80% diesel)
- 250 E85 flex-fuel vehicles capable of being fueled with ethanol
- 91 hybrid Ford Escape SUVs
- 40 Prius hybrids
- 10 Prius Plug-in hybrid electrical vehicles (PHEV)
- 2 biodiesel-electric hybrid bucket truck
- 1 liquid petroleum gas (LPG) bucket truck

Staff Ex. 2.0 at 9-10. As such, alternative-fuel vehicles represent 63 percent of ComEd's total fleet of cars and trucks. *Id.*

The Proposed Order correctly assessed this evidence and appropriately concluded that "Because of the problems with the budget process, ComEd has not shown that the proposed EV pilot, which the Commission finds to be poorly defined, should be funded through Rate ACEP. Proposed Order at 93. That finding should be sustained in the Final Order.

C. Low-Income Customer Assistance Programs

ComEd describes its Low-Income Assistance Programs ("LIAP") as more than just a pass-through of costs, as the Proposed Order has characterized this aspect of Rate ACEP. ComEd BOE 26-27. The Company asserts that LIAP will in fact help lower uncollectibles expense, reducing long-term uncollectible costs by rewarding customers who do not qualify for Low Income Home Energy Assistance Programs for timely payments, and thereby reducing Rider UF charges. ComEd BOE at 27. ComEd concludes that its LIAP is therefore "beneficial for all ratepayers." *Id.*

The Proposed Order agrees that these programs are beneficial to ComEd's qualifying low income customers, and perhaps even to all of the Company delivery service customers, but only

assuming that they reduce the Company's uncollectibles *and* that ratepayers do not have to pay for them. If ratepayer funding is required, the Proposed Order concludes that this proposal represents nothing more than a rate increase for the majority of ComEd's customers, with "no net benefits to customers as a whole." Proposed Order at 63. As such, the Proposed Order continues, the LIAP results in "an inappropriate shifting of costs from one group to another." *Id.*

ComEd argues that Rate ACEP is needed to put LIAP into place "to eliminate after-the-fact disputes about legality and recoverability of costs." ComEd BOE at 28. Yet ComEd provides no explanation of what issues of legality or cost recovery LIAP introduces that can *only* be resolved through alternative regulation. Nor does the Company supply any analysis of the effectiveness of current programs in reducing uncollectibles, how the proposed programs are designed to address ComEd's unique uncollectible problems or how funding should be coordinated with existing financial assistance programs. *See* AARP BOE at 17. The Company has not demonstrated any particular need to provide LIAP as part of Rate ACEP, and consequently, as AG witness Brosch observes, "there is no reason such programs could not be made available under traditional rate case regulation with funding by Exelon shareholders rather than ratepayers." AG Ex. 1.0 at 31. The Proposed Order's evaluation reaches a similar conclusion, noting that "ComEd proposes to pass through \$10 million annually in CARE costs to ratepayers. There is no budget that ComEd is trying to beat and there is no reduction in O&M expenses." Proposed Order at 64. In short, there is nothing about ComEd's LIAP that qualifies it for special treatment as alternative regulation.

D. Cost Recovery Mechanism for Future Smart Grid Investments

ComEd disputes the Proposed Order's conclusion that adopting a smart grid cost recovery mechanism, such as Rate ACEP, is premature, as well as the ALJ's finding that such a decision is appropriately addressed in the upcoming smart grid Policy Docket. ComEd BOE at

29. The Company asserts that “the policy docket is just that – a proceeding to discuss the policy surrounding Smart Grid investments, not cost recovery mechanisms.” *Id.*

ComEd is wrong. While the Policy Docket has not been initiated as of this date, issues surrounding cost recovery are likely to be included in the proceeding. Indeed, the October, 2010 Smart Grid Collaborative Report, which was issued as a part of the smart grid exploration process approved by the Commission in Docket No. 07-0566, included a discussion of cost recovery possibilities in an attempt to reflect the participants’ views on this controversial subject. *See, Illinois Statewide Smart Grid Collaborative Report*, issued October 1, 2010 at 25, 30-31, 255-257. The fact that no consensus was reached on this important aspect of smart grid evaluation beckons the Commission to explore the topic in the Policy Docket. The Proposed Order correctly concluded that approving a cost recovery mechanism without the Commission’s evaluation of cost recovery proposals in the Policy Docket would contradict the full smart grid evaluation process outlined in the Commission’s Order in Docket No. 07-0566. Proposed Order at 99-100. As the Proposed Order aptly states, “By following the defined process, the Commission will not put the State behind in the Smart Grid discussion going on throughout the nation, as suggested by ComEd witness Hemphill, but rather it will allow the Commission to maintain control over the discussion.” *Id.* at 100.

Moreover, a recent Illinois Appellate Court ruling that specifically examined the Commission’s approval of ComEd’s last attempt to isolate smart grid costs through a discrete cost recovery mechanism supports a finding that Rate ACEP is unlawful single-issue ratemaking, and an inappropriate mechanism for funding smart grid. In *Commonwealth Edison Co. v. Illinois*

Commerce Comm'n, (“*ComEd*”), 937 N.E.2d 685 (2d Dist. 2010),⁸ the Court ruled that a rider was not an appropriate way to recover the costs of AMI meters and other plant investment. Because riders always permit direct recovery of a single cost, rather than incorporating that cost into the aggregate calculation of the revenue requirement, they always pose, at the very least, a “danger of single-issue ratemaking.” *ComEd*, 937 N.E.2d at 687, citing *City of Chicago II*, 281 Ill. App. 3d at 628; see also *ComEd*, 937 N.E.2d at 708 (“Because a rider is a method of single-issue ratemaking, by nature, it is not allowed absent a showing of exceptional circumstances.”). Every Illinois court to review a non-statutory Commission-approved rider has judged it against the limits established by the rule against single-issue ratemaking. In *ComEd*, the court comprehensively reviewed all of the Illinois judicial decisions involving riders, and identified the general principles that bind these cases into a uniform legal standard. The Court concluded that exceptional circumstances necessary to justify a rider arise only when the proposed rider is designed to “recover a particular cost if (1) the *cost* is imposed upon the utility by an external circumstance over which the utility has no control and (2) the *cost* does not affect the utility’s revenue requirement.” *Id.* at 687 (emphasis added). The Court further held:

In other words, a rider is appropriate only if the utility cannot influence the cost (*Citizens Utility Board*, 166 Ill.2d at 138 [‘a rider mechanism is effective and appropriate for cost recovery when a utility is faced with unexpected, volatile, or fluctuating expenses’) and the expense is a pass-through item that does not change *other expenses or increase income* (*Citizens Utility Board*, 166 Ill.2d at 138 (*a valid rider has no ‘direct impact on the utility’s rate of return’*)).

Id. at 687. In each instance in which a Court upheld the use of a rider as a cost recovery mechanism, the expense was an externality imposed on the utility, and the expense was passed directly on to the consumer without affecting the utility’s return on investment. *Id.* at 688.

⁸ The Illinois Supreme Court last month rejected *ComEd*’s and the Commission’s petitions for leave to appeal the Second District ruling.

While ComEd won't call it a rider, Rate ACEP functions in the same piecemeal way, and does not pass the two-part test established in *ComEd*. Like the rider deemed illegal in *ComEd*, Rate ACEP is proposed to be used for the recovery of plant investment, and in particular, smart grid investment. The costs for the Rate ACEP projects are not "imposed upon the utility by an external circumstance over which the utility has no control." *Id.* at 687. The Rate ACEP proposal does not collect revenues for a pass-through item, but rather would "increase income", thereby affecting its revenue requirement. *Id.* In its rejection of Rider SMP, the *ComEd* Court highlighted the fact that ComEd expected smart grid system modernization to generate operational efficiencies, and Rider SMP's failure to recognize that "the increased costs (of smart grid investments) would be more than offset by a positive, corresponding change in another component of the revenue requirement formula." *Id.* at 688. The Court noted: "To allow Rider SMP would be to improperly consider in isolation changes in a particular portion of a utility's revenue requirement." *Id.*, citing *Business and Professional People for the Public Interest v. Illinois Commerce Comm'n*, 146 Ill. 2d 175, 244 (1991). Rate ACEP similarly increases rates for projects in isolation of a utility's revenue requirement, and includes no mechanism for sharing or offsetting positive O&M savings that ComEd claims smart grid technologies engender.

For all of these reasons, the Proposed Order was correct in its conclusion that approving a smart grid recovery mechanism now – before the Commission has even explored whether an extraordinary cost recovery mechanism is needed – is ill-advised.

III. THE PROPOSED ORDER CORRECTLY CONCLUDED THAT THE COMED RATE ACEP PROPOSAL FAILED TO MEET THE STATUTORY CRITERIA.

A. Contrary to ComEd's Assertions, the Proposed Order Does *Not* Restrict the Commission's Authority Under Section 9-244 of the Act.

In yet another strawman argument, ComEd complains that the wrongly interprets Section 9-244(a) of the Act, “reads non-existent limitations into the types of alternative regulation programs authorized” and that “the upshot of the proposed rulings is that virtually no alternative regulation proposal would be lawful – even the Nicor proposal that the Commission approved a decade ago.” ComEd BOE at 36. ComEd’s complaint is based on its assessment that its Rate ACEP proposal falls under both subsections (i) and (ii) of Section 9-244(a). *Id.* at 38. In asserting as much, the Company argues first that Section 9-244 authorizes alternative regulation *programs*, and does not limit those programs to “entire utility services.” *Id.*

This argument again mischaracterizes the analysis of the Proposed Order at pages 18-21, as well as Section 9-244 of the Act. Merely because ComEd called its Rate ACEP proposal a “program” doesn’t mean that it qualifies under Section 9-244(a)(i) as an alternative regulation program. Section 9-244 of the Act permits the Commission to:

...authorize for some or all of the regulated services of that utility, the implementation of one or more programs consisting of (i) alternatives to rate of return regulation, including but not limited to earnings sharing, rate moratoria, price caps or flexible rate options, or (ii) other regulatory mechanisms that reward or penalize the utility through the adjustment of rates based on utility performance. In the case of other regulatory mechanisms that reward or penalize utilities through the adjustment of rates based on utility performance, the utility's performance shall be compared to standards established in the Commission order authorizing the implementation of other regulatory mechanisms.

220 ILCS 5/9-244(a). Given that ComEd will continue to file traditional rate cases under its Rate ACEP proposal, the Proposed Order correctly concluded that ComEd’s petition fits neither category listed under Section 9-244(a). 220 ILCS 5/9-224(a). Whether the Rate ACEP projects are identified as programs or services, the proposal fails to qualify as alternative regulation, as all of the Staff and Intervenor witnesses evaluating the proposal concluded. As the Proposed Order

correctly noted, “Although ComEd states that Rate ACEP is really a combination of both (i) and (ii), the Commission does not find ComEd’s Rate ACEP to fall under option (i). Ratepayers that will receive the “service” chosen by ComEd for its Alt Reg petition will still take service under its traditional rate of return tariffs. Rate ACEP charges will be *in addition to* customers’ base rates, not in the alternative.” PO at 18 (emphasis added). Requiring ratepayers to pay an additional charge for new “programs” that are nothing more than an expansion of existing O&M and plant expenses is not “an alternative to rate of return regulation.” 220 ILCS 5/9-244(a)(i).

In addition, the Proposed Order presented a sound rationale for its conclusion that the Rate ACEP proposal did not quite fit under Section 9-244(a)(ii) either. The Proposed Order states:

This option requires a finding that the “service” provided under Rate ACEP will be compared to performance standards, which the Commission must herein adopt. As noted, the “services” proposed by ComEd are certain utility investments and associated expenses. The “standard” proposed by ComEd for assessing its performance of the “service” is whether or not ComEd will be able to beat its budget for the investments. To say that ComEd’s performance for Rate ACEP “services” can be judged by whether it beats its own budget, even if approved by the Commission, does not seem consistent with what is contemplated by the statute - adjustments to rates based on utility performance. ...In the Commission’s view, Rate ACEP is a supplement to traditional rate of return regulation and because it provides for recovery of operating expense, capital expenditures and associated carrying charges it may not be fairly characterized as an alternative to rate of return regulation.

Proposed Order at 19. Contrary to ComEd’s strawman argument that the Proposed Order “seems troubled and confused” about the distinction between “programs” and “services,” the ALJ correctly applied Section 9-244 in its entirety, and recognized the requirement in Section 9-244(b) that require the Commission to compare the “program” with what “would have been in effect under traditional rate of return regulation for the *services* covered by the program...” 220 ILCS 9-244(b). While ComEd continues to reference the *Nicor Alt Reg Order* as an apt precedent for its proposal, the Company ignores the fact, as the Proposed Order correctly noted,

that that decision affected rates for a particular service – gas supply – which has a separate rate and service classification attached to it. The same cannot be said for UUFR projects, utility-owned electric vehicles and low income program expenses, which are merely categories of O&M and capital costs currently subsumed in ComEd’s revenue requirement. ComEd accuses the Proposed Order of being “unclear about what utility service ComEd’s proposed programs relate to.” ComEd BOE at 37. On the contrary, there is nothing unclear about the Proposed Order’s conclusion that in fact these programs are *not* services. ComEd’s claim that these O&M expense and capital cost categories are somehow “services” under Section 9-244(b)’s use of the word is nothing more than strained, legal rhetoric.

The Company also observes that the Proposed Order’s conclusion at page 18 that it fits neither category of alternative regulatory programs listed in subsection 9-244(a) “appears to view the fact that ComEd’s programs also have other goals besides cutting costs in response to the reward/penalty mechanism somehow invalidates their status as alternative regulation programs” ComEd BOE at 38-39. This assessment is equally suspect. A proposal to increase customer rates – above and beyond those set in a traditional rate case – for discrete “projects” that are nothing more than expansions of O&M and capital cost categories is *not* alternative regulation. It likewise, is not comparable to the ill-fated *Nicor Alt Reg* plan. Nothing in Section 9-244 permits the Rate ACEP adjustments proposed by ComEd – no matter how often ComEd calls it alternative regulation.

Section 9-244 (b) provides very explicit review criteria for a proposed program of alternative regulation. According to the statute, the Commission must find, based on the record, that all of the review criteria have been satisfied in order to approve such a program. 220 ILCS

5/9-244(b). A discussion of those criteria, and the Proposed Order's analysis of the criteria, follows below in response to ComEd's specific criticisms.

B. The Proposed Order Correctly Interpreted Section 9-244(b) of the Act.

1. Rate ACEP Fails Section 9-244(b)(1) of the Act.

At page 39 of its BOE, ComEd again claims that the Proposed Order misapplies the plain language of Section 9-244. The Company states that the Commission's analysis calls for a comparison between rates under the proposed alternative regulation plan "and the rates that 'otherwise would have been in effect' under traditional regulation to recover the costs of the *same* 'services covered by the program.'" ComEd BOE at 39 (emphasis added). ComEd's insertion of the word "same" in its assessment of the statutory analysis alters the assessment required under Section 9-244(b)(1). It then states that "the question of whether rates would be lower than if the Commission rejected ComEd's proposal entirely is utterly irrelevant to Section 9-244(b)(1)." *Id.*

ComEd is wrong. The Proposed Order got it exactly right when it highlighted the fact that ComEd asks this Commission to compare its Rate ACEP proposal "to a hypothetical situation that has never happened in the past and seems unlikely to happen in the future." Proposed Order at 33. The Proposed Order states:

Under Section 9-244(b)(1), the Commission must compare rates under Rate ACEP with rates under traditional rate of return regulation. ComEd argues that the regulatory lag that is inherent to traditional regulation is not relevant to the question under Section 9-244(b)(1). ComEd argues that the Commission, when comparing Rate ACEP to traditional regulation, should look at what rates would be if ComEd annually filed a general rate case with a future test year – where customers would receive no 5% credit and the realization of savings would await the next general rate case.

The Commission concludes that ComEd's position is inconsistent with the statutory language. The rates under alternative regulation are to be compared to the rates that "would have been in effect under traditional rate of return regulation." Section 9-244(b)(1). The Commission finds that ComEd's position ignores that generally under "traditional rate of return regulation" the rates remain in effect for a number of years. Under traditional rate of return regulation, ratepayers would be assessed no O&M expenses or carrying costs for these projects until the next rate case. Although ComEd accuses Staff of treating this as a discount to rates under traditional regulation, the Commission believes that ComEd fails to consider that this constitutes a real ratepayer benefit and protection under traditional rate of return regulation. See ComEd RB at 48-49.

Proposed Order at 33.

ComEd's parsing of Section 9-244(b)(1) suggests that ComEd will be providing some different service than the existing electric delivery service if Rate ACEP is approved, where the Company inserts the word "same" in its analysis of the statute. As AG witness Brosch noted, there is no change in the quality or quantity of energy deliveries that ComEd would provide with or without Rate ACEP. AG Ex. 3.0 at 13.

The only way that Rate ACEP can compare favorably to traditional ratemaking from a customer impact perspective is if the Commission assumes continuous regulation and no regulatory lag. This is a flawed assumption because traditional regulation involves periodic consideration of all costs and revenues within a test year to establish the revenue requirement. Mr. Brosch rejected as specious ComEd witness Hemphill's suggestion that the same changes in costs for the proposed projects would translate immediately into higher rates under both traditional regulation and Rate ACEP, resulting in the 95 percent expense limitation and overall budget constraints producing claimed "lower rates" for customers. AG Ex. 3.0 at 12-14.

ComEd also opines that traditional regulation creates "a fundamental unjustness" as a result of the regulatory lag that occurs once rates are set, "making recovery of its capital expense significantly delayed and its O&M expenses denied if they do not occur in a rate case test year." ComEd BOE at 41. This claim is simply bunk. Under traditional regulation, the utility selects a

test year and presents a calculation of its desired revenue requirement, including operating expenses (including depreciation and taxes) plus a rate of return applied to a rate base measure of invested capital. The key characteristics of traditional rate case regulation include:

- A **test year**, in which all of the components of the revenue requirement are holistically analyzed and quantified in a balanced and internally consistent manner with appropriate “matching” of costs and revenues.
- Utilization of regulatory lag as an **efficiency incentive**, by financially rewarding the utility for achieved cost reductions and punishing the utility when costs increase more rapidly than revenues between test years.
- Application of **regulatory rules** to the analysis of revenue requirement components, including prescribed adjustments, minimum filing requirements, and adherence to past rate orders and policies.
- A detailed **formal filing** with testimony and exhibits supportive of the asserted revenue requirement.
- Updated quantification of most or all elements of the revenue requirement, in a **holistic measurement** of changing revenue requirements, including studies of the current cost of capital,
- An opportunity for **prudence review** of management actions or inaction that may have contributed to unreasonable recorded costs.
- **Procedural provisions** for discovery and critical analysis of test year data submitted by the utility, and for litigation of disputed issues.
- **Comprehensive Review** of utility filings, discovery and submission of testimony and exhibits by Commission Staff and consumer intervenors such as the People of the State of Illinois.
- **Regulatory costs** to support these more formal procedures.

AG Ex. 1.0 at 5-6. As noted earlier in this Brief, the fundamental basis for traditional utility regulation is that, in the absence of competitive markets to determine pricing for an essential public service, just and reasonable utility rates should be determined based primarily upon the utility’s prudently incurred costs to provide such monopoly services. *Id.* ComEd’s characterization of this process as fundamentally unfair ignores the fact that rates are set under traditional regulation to provide the utility with a revenue stream to “match” a utility’s reported

costs and revenues based upon a test year. There is nothing unjust about that process, which has functioned well for more than a century.

Rider ACEP, on the other hand, is designed and intended to reduce regulatory lag, by translating project costs into higher rates to customers between traditional rate cases without discernible benefits. That fact belies any suggestion that the ComEd program “is likely to result in rates lower than otherwise would have been in effect under traditional rate of return regulation for the services covered by the program... .” 220 ILCS 5/9-244(b)(1).

2. Rate ACEP Fails Section 9-244(b)(2) of the Act.

ComEd next attacks the Proposed Order’s conclusion that the Rate ACEP proposal fails to satisfy Section 9-244(b)(2) of the Act. ComEd opines that both the Rate ACEP mechanism and the projects it supports provide substantial and identifiable benefits. ComEd BOE at 44. Again, the Company twists the meaning of the words used in the Proposed Order’s analysis of this statutory criterion. ComEd takes issue with the Proposed Order’s conclusion that “it is the Rate ACEP mechanism itself that must provide benefits to ratepayers that would not otherwise be available.” Proposed Order at 40. That observation is *not* contrary to the statute.

Section 9-244 falls within the ratemaking provisions of Article IX of the Act. The Commission, accordingly, must conclude under Section 9-244(b)(2) that the Rate ACEP mechanism will benefit ratepayers. 220 ILCS 5/9-244(b)(2). Having said that, the Proposed Order, contrary to ComEd’s claims, does not fail to examine the alleged benefits of each of the Rate ACEP programs. At page 41 (and indeed, in earlier sections of the Proposed Order) the ALJ assessed the alleged merits of the UUFR, electric vehicle pilot and low income proposals. Based on the evidence cited, it found them lacking.

Second, ComEd's argument that any recognized benefits of the low income proposal "cannot be undone just because the costs of delivering that benefit are paid for." ComEd BOE at 45. The People submit that who pays for those benefits *is* relevant to the overall determination of whether this particular proposal provides the kind of substantial and identifiable benefits Section 9-244(b)(2) envisions. As discussed above, and in the People's other Briefs, financing the programs via Rate ACEP diminishes any conclusion that the programs deliver benefits.

It is not enough to assert that benefits will be created by investing in these programs because if the Rate ACEP program is not approved the projects will not be pursued. The Commission Staff rightly points out that ComEd's interpretation of Section 9-244(b)(2) is a tautology (the benefits are likely to occur because if the program is not approved, the projects would not be implemented and any program benefits would not be realized). Staff Brief at 55. There must be a context for assessing alleged benefits. The costs and benefits from the other three proposed programs can readily be addressed and realized under traditional regulation without Rate ACEP, as described in Part II of the AG Initial Brief. *See* AG Initial Brief at 8-24.

The overwhelming, substantial evidence of the record supports a finding that ComEd's proposal does *not* satisfy Section 9-244(b)(2) of the Act, as the Proposed Order rightly concluded.

3. Rate ACEP Fails Section 9-244(b)(7) of the Act.

Under Section 9-244(b)(7), any alternative regulation program must include annual reporting requirements and other provisions that will enable the Commission to adequately monitor its implementation of the program. In the AG briefs, the People highlighted the fact that ComEd's proposal would require the Commission to play what is characterized as in its Petition

as a “central role in determining the direction ComEd will take with future investments in Smart Grid technology, accelerated underground facility reinvestment, and EV, as well as low income assistance.”⁹ Given the amount of analysis Staff and Intervenors must accomplish in reviewing any Rate ACEP project proposals, as well as the short time frames (five months) envisioned for the formal Commission proceedings, it is unlikely that the Commission can effectively play “a central role” in determining ComEd’s investments. *See* AG Initial Brief at 31-35. In addition, the Commission’s review is limited to the proposed projects and budgets offered by the Company and the constraints of the administrative process. ComEd’s reports regarding how it performed in comparison to the budgets it sets are, for the reasons discussed above and in the AG Initial and Reply Briefs, not meaningful information to evaluate program performance.

The Proposed Order agreed with this point. Proposed Order at 45. ComEd objects, arguing that the ALJ’s mention that “perhaps additional information regarding whether the investments were prudently made” and information quantifying benefits made would also be beneficial in evaluating Rate ACEP. *Id.* ComEd is correct in noting that the Commission cannot adopt a hindsight prudence assessment of the investments if it has originally granted approval of the projects under the Rate ACEP mechanism. However, the Commission could presumably assess the reasonableness of the expenses incurred under a Rate ACEP reconciliation proceeding if the mechanism was adopted. Engaging in such suppositions is irrelevant, however, given the defects in Rate ACEP that fail to satisfy the particular criteria of Section 9-244(b), in this case, Section 9-244(b)(7). As noted earlier in this and other AG briefs, the budget information provided is simply inadequate for the Commission to “monitor its implementation of the program”. 220 ILCS 5/9-244(b)(7); AG Initial Brief at 55-57; AG Reply Brief at 50-51.

⁹ ComEd Verified Petition at page 12.

4. Rate ACEP Fails Section 9-244(b)(8) of the Act.

Section 9-244(b)(8) of the Act provides that “the program includes provisions for equitable sharing of any net economic benefits between the utility and its customers to the extent the program is likely to result in such benefits.” 220 ILCS 9-224(b)(8). In its BOE, ComEd argues again that the Proposed Order again applies the wrong legal standard, suggesting that the ALJ failed to understand that a finding that benefits exist is not required under Section 9-244(b)(8). ComEd BOE at 48.

The Proposed Order is clear on the proper analysis, when it states, “To make this determination it must first be determined if there are net economic benefits associated with implementing Rate ACEP.” Proposed Order at 50. The Proposed Order then goes on to state:

If the Rate ACEP mechanism is considered in conjunction with the programs proposed for recovery thereunder, as ComEd would have the Commission do, there might be net economic benefits. The Commission is concerned that the benefits, however, are loosely defined and totally unquantified. Moreover, the Commission is concerned that any efficiencies that will be gained will not be realized by customers until ComEd’s next rate case. So, although Rate ACEP allows for the immediate recovery of O&M expenses it does not immediately reflect the potential savings and thus, the Commission believes any net economic benefits are not equitably shared with customers.

Id. The Proposed Order then proceeds to assess each Rate ACEP program and whether benefits are, in fact, equitably shared. *Id.* at 50-51. In no way did the ALJ assume that Section 9-244(b)(8) required economic benefits.

ComEd further reiterates its position that under Rate ACEP, customers get a guaranteed 5% O&M credit and shared efficiency benefits, on top of program benefits. ComEd BOE at 49. Here again, however, the Company applies its assumption that the budget baseline that serves as the metric for establishing alleged customer benefits is a workable metric. That assumption is

not supported by the evidence, as discussed earlier in this Brief. AG witness Brosch characterized the Rate ACEP proposal *not* as equitable sharing, but rather an aggressive recovery of, and conversion of, discretionary costs into new revenues for ComEd, rather than an “equitable sharing”. AG Ex. 1.0 at 34. The EV program is a pilot, for which any economic benefits are uncertain and for which ComEd’s proposal would shift costs and risks to ratepayers and away from shareholders. If the UUFR produces any net economic benefits, through reduced outages and outage response costs, the resulting cost savings would not be shared with ratepayers until they are captured within a future rate case test year.

Mr. Colton explains in his testimony why recovery of low income assistance program costs from ratepayers is inequitable. The inescapable message he delivers is that ComEd, along with its Exelon parent and generation affiliate, having spent significant amounts to support ComEd CARE over the past five years, cannot now argue that continuing to offer bill payment customer assistance programs is a corporate burden so great that it must ask ratepayers to bear even higher rates to fund what its independent judgment embraced years ago as a reasonable expenditure, and in the same breath argue that this is a significant benefit to ratepayers. AG Ex. 2.0 at 37-50.

Finally, ComEd argues that the Proposed Order’s rejection of the budget-based incentive mechanism in Rate ACEP “is not a reason to criticize the sharing features of the proposal.” ComEd BOE at 50. The problem with this view, however, is that the budget-based incentive mechanism is a basis for at least a portion of the sharing provisions in the Rate ACEP proposal. The Proposed Order correctly recognized this fact, when it noted, “It appears to the Commission that every time ComEd spends less than 95% of its proposed budget, ratepayers pay more than ComEd’s actual costs. This is further exacerbated by the failure to share savings from gains in

efficiencies until its next rate case. Accordingly, the Commission finds that ComEd has not shown that Rate ACEP includes provisions for an equitable sharing of any net economic benefits between the utility and its customers to the extent the program is likely to result in such benefits.” The budget mechanism simply cannot be ignored when the Commission makes its 9-244(b)(8) assessment.

For all of these reasons, ComEd’s arguments that the Proposed Order incorrectly applied Section 9-244(b)(8) to the Rate ACEP proposals should be rejected.

IV. CONCLUSION

WHEREFORE, the for the foregoing reasons, the People request that the Commission reject Rate ACEP and enter an Order consistent with the recommendations included in the Proposed Order, as modified in the People’s Brief on Exceptions.

Respectfully submitted,

The People of the State of Illinois
by LISA MADIGAN, Attorney General

_____/s/_____
Janice A. Dale, Chief, Public Utilities Bureau
Susan L. Satter, Senior Assistant Attorney General
Karen L. Lusson, Senior Assistant Attorney General
Michael R. Borovik, Assistant Attorney General
100 W. Randolph St., 11th Floor
Chicago, IL 60601
Telephone (312) 814-3736
Fax (312) 814-3212
Email: jdale@atg.state.il.us
Email: ssatter@atg.state.il.us
Email: klusson@atg.state.il.us
Email: mborovik@atg.state.il.us

Dated: April 26, 2011